MINUTES
of the
SIXTH MEETING
of the
INVESTMENTS AND PENSIONS OVERSIGHT COMMITTEE

November 7, 2007
State Capitol
Santa Fe

The sixth meeting of the Investments and Pensions Oversight Committee (IPOC) for the 2007 interim was called to order by Senator John Arthur Smith, chair, on Wednesday, November 7, 2007, at 10:15 a.m. at the State Capitol in Santa Fe.

Present
Sen. John Arthur Smith, Chair
Rep. Donald E. Bratton
Rep. Larry A. Larrañaga
Sen. Mary Kay Papen
Rep. Henry Kiki Saavedra
Rep. Jim R. Trujillo
Rep. Luciano "Lucky" Varela

Absent
Rep. John A. Heaton, Vice Chair
Sen. Joseph J. Carraro
Sen. Phil A. Griego
Sen. Carroll H. Leavell

Advisory Members
Rep. Andrew J. Barreras
Sen. Carlos R. Cisneros
Rep. Miguel P. Garcia
Bob Gish, Public Employees Retirement Association
James Lewis, State Treasurer
Olivia Padilla-Jackson, State Board of Finance
Rep. Jane E. Powdrell-Culbert
Sen. Leonard Lee Rawson
Charles Wollman for Gary Bland, State Investment Council

Sen. Pete Campos
Sen. Stuart Ingle
Bob Jacksha, Educational Retirement Board
Rep. Patricia A. Lundstrom
Rep. John Pena
Sen. Michael S. Sanchez
Sen. H. Diane Snyder
Rep. Sheryl Williams Stapleton
Rep. Eric A. Youngberg

Staff
Doris Faust, Legislative Council Service (LCS)
Cleo Griffith, LCS
Stephanie Schardin, Legislative Finance Committee (LFC)
Doug Williams, LCS

Guests
The guest list is in the meeting file.

Wednesday, November 7

The committee adopted the minutes of the October 17, 2007 meeting.

Retiree Health Care Authority; Report of the HB 728 Group
—David Abbey, Director, LFC
—Stephanie Lenhart, Department of Finance and Administration
—Danielle Wilson, Chair, Retiree Health Care Authority (RHCA) Board

The RHCA was created in 1990 to provide health insurance benefits to eligible retirees, their spouses and dependents of certain public participating entities. RHCA was prefunded for six months prior to providing benefits. This brief period is in contrast to other retirement benefits for state employees that had much longer periods before benefits were paid out, and this has had significant ramifications as discussed below.

The RHCA provides benefits to approximately 42,000 members and has an annual budget for FY08 of $216,628,900. The RHCA is governed by an 11-member Board of Directors (Board) comprised of representatives of retirees, current employees and public employers. The Board sets overall policy for the agency, oversees the procurement of insurance benefits and approves premium adjustments and benefit designs.

The RHCA is facing three significant challenges. The first is the projected future insolvency of the RHCA Fund in as few as seven years because annual revenues have fallen short of expenditures, and RHCA has taken funding from its reserves and long-term investments to cover costs. The second challenge is that new accounting standards now require the state to publish the unfunded liability associated with nonpension retirement benefits and a significant unfunded actuarial accrued liability could eventually affect the state's bond rating. Finally, because of increasing medical costs and increasing numbers of retirees entering the system, little if any prefunding of benefits is occurring, thereby leaving the future viability of the system in doubt.

In 2006 and many previous years, the solvency of the RHCA Fund was projected by contracted actuaries to be 25 years. However, as of September 2007, the solvency was projected to be seven years, with insolvency anticipated to occur by June 30, 2014 unless significant changes are made to the system. This dramatic revision in the solvency estimates was the result of a change in the expected program participation rate, which was increased from 35% to 75%. In other words, for many years, RHCA and the state of New Mexico have been operating under an inadequate participation assumption resulting in unrealistic projections of the financial stability and long-term viability of the system.

Additionally, in 2004 the General Accounting Standards Board (GASB) issued Statements 45 and 43 requiring that states and other governmental entities publish, as part of their audited financial statements, their unfunded actuarial accrued liability (UAAL) for nonpension retirement benefits such as health insurance. Initial estimates of New Mexico's UAAL were as high as $5 billion. The level of UAAL depends on the amount of annual revenue received and whether or not the fund it is placed in is an irrevocable trust or its equivalent, thereby allowing the state to take advantage of a lower discount rate. Based upon the presumption that the RHCA operates as an "equivalent arrangement" to an irrevocable trust, the most recent estimates place New Mexico's UAAL at $4.1 billion. However, the annual required contribution (ARC) necessary to prefund the state's current obligation is $373.9 million without interest. It should be noted that the gap between the ARC necessary to fund fully the UAAL over 30 years and the forecasted FY08 budget is $200.5 million.

In 2007, the legislature passed HB 728, introduced by Representative Varela, that established a work group to study how to preserve health care benefits for retirees. HB 728 also appropriated an additional $3 million per year for fiscal years 2008 through 2010 to the existing flow of revenue to the RHCA from the suspense fund. Membership in the work group included the Office of the Governor, the Department of Finance and Administration, the LFC, the LCS and staff and Board members from the RHCA.

HB 728 tasked the work group to:

- examine the long-term actuarial trend and condition of the RHCA Fund;
- examine the equitable nature of the current contribution rates between retirees and current employees;
- determine the percent of the fund balance derived from state sources versus the percent derived from the sources of political subdivisions, compare those percentages with the expenditures from the fund for state retirees versus retirees of the political subdivisions and study the feasibility of creating two separate programs for the two classes of retirees;
- examine options to improve the actuarial soundness of the RHCA Fund; and
- evaluate the need for, and the feasibility of, securing the RHCA Fund as an irrevocable trust.

In order to extend the solvency period and to reduce New Mexico's UAAL, the HB 728 work group considered a wide range of options. While the RHCA Board has general authority to make changes in areas such as premiums and benefit design, other changes, such as increasing the employer/employee contribution, require legislative action. Therefore, the work group placed recommendations in the following categories: changes recently enacted by the RHCA Board, recommendations that would increase the fund by $4 million or more, recommendations that would increase the fund by $2 million to $4 million, low-impact recommendations of $2 million or less and recommendations for future consideration.

In August 2007, the RHCA Board approved a number of measures intended to extend the solvency period. The Board:

- moved the self-funded Medicare prescription drug coverage to an RHCA-sponsored prescription drug plan;

- adjusted benefit designs, including increases to certain co-payments and out-of-pocket expenses; and
- approved an average 9% increase in premiums across the benefit plans while committing to tying future premium increases to medical and pharmacy trends.

In addition to the changes enacted by the RHCA Board, the work group agreed on the following recommendations that, if enacted, are expected to extend the solvency period to 17.5 years at an assumed ultimate annual health care trend rate of 8% for FY10 and after, and add approximately $54 million in revenues.

- Focus on solvency, ARC and UAAL: Develop a comprehensive set of actions that will focus not only on extending solvency but also significant prefunding for future retirees and reducing the UAAL, thereby protecting the state's financial position.
- Solvency period: Establish a 25-year solvency period with provision for regular adjustments to premiums and other revenue streams that maintain that solvency period going forward.
- Employer/employee contribution increase: Increase the employer/employee contribution to a total of 2.4% of pay for nonpublic safety personnel and 3.0% for public safety personnel to recognize the fact that full retirement is earned for the latter after 20 years rather than 25. The current employer/employee contribution is a total of 1.95% of pay based on 1.3% of pay for the employer share and .65% of pay for the employee share, with the recommended increase to a total of 2.4% pay resulting in partial prefunding of unfunded liabilities for active employees.
- Suspense fund allocation: Extend the $3 million per year increase from the suspense fund that was authorized in HB 728. For nonstate participating entities, assess an equivalent percentage of their general revenue.
- Adjust retiree and spouse subsidies: Require a retiree's cost share for the base benefit plans to 50% of projected costs and 75% for spouses (current average is 32.4% for retirees and 52.4% for spouses). It is further recommended that the subsidy percentage for the base plans be set in statute.
- Age and service adjustments: Implement the rule of 70 for public safety retirees and rule of 80 for all other retirees effective January 1, 2009. Rule of 70 means that a retiree's age plus years of service must equal 70 or greater before benefits can be taken.
- In addition to these changes, the HB 728 work group recommends the following changes that, while not having significant impact on the long-term solvency or UAAL, will improve the operations of the RHCA and the prospects for the state's retiree health care system:
    - Board composition: Rebalance the Board to add representation by the secretary of finance and administration and increase active employee representatives.
    - Annual GASB valuations and solvency modeling: Provide annual valuations each December 31 to the legislature that update GASB

43 disclosures and long-term solvency projections and model the impact of changes being recommended by the RHCA Board (including the expected impact of the total package of changes on the UAAL).

- Health and disease management: Provide health and disease management programs from contracted insurance vendors that include measurable health outcomes and mandate health risk assessments for members as a condition of initial and ongoing enrollment.
- Statewide consolidation: Explore economies of scale that can be gained from consolidating administrative functions of the RHCA, the General Services Department's Group Benefits Division, other smaller publicly financed health insurance pools, the Public School Insurance Authority and the Albuquerque Public Schools.
- Attestation requirement: Require that all enrollees attest that they are not eligible for other health care coverage due to other employment as a condition of initial and ongoing enrollment.

No single action by the executive, the legislature or the RHCA will restore the balance needed to the current retiree health insurance system. The HB 728 work group realized early on in its study that all participants in the system, the retirees, active employees and employers, will need to participate in addressing the state's unfunded liability and in moving the system into permanent solvency. While it is not feasible or prudent to prefund fully the program in a single year, the work group developed short-term recommendations to move the system into solvency and longer-term recommendations that will need to be considered as the state develops an approach for addressing the ARC and UAAL in a manner and over a time period that is fiscally responsible.

Representative Bratton expressed concern over the 8% growth rate used for projecting health care costs. Mr. Abbey responded that the actuary used 8% over the 30-year projection based on the reality that health care costs cannot continue to grow in double digits or else health care will consume the entire economy. Marie Thames, executive director, RHCA, stated that current actual growth is 9%, and the actuary used a 9% growth for the first five years and then 8% for the balance of the projection.

Senator Smith requested staff to explore the possibility of scheduling one additional meeting to consider the RHCA-proposed legislation.

Representative Larrañaga asked if nonstate participating employers can have their employer contribution increased by action of the RHCA Board. Ms. Wilson responded that legislation would be required.

Representative Trujillo observed that creation of a universal health care plan can have an impact on the RHCA.

Senator Smith expressed concern that difficulties with the RHCA might be used during the upcoming legislative session to rush into health care legislation.

Senator Smith asked the committee if anyone had thoughts on adopting a rule of 70 for retirees receiving RHCA benefits. There was no response.

Public Employees Retirement Association (PERA); Actuarial Update
—Terry Slattery, Executive Director, PERA

The PERA statutory obligations are:

- pension payments to current and future retired members and vested former members;
- survivor pension beneficiaries; and
- refunds of member contributions to nonvested former members and administrative and investment expenses incurred in the operation of the PERA.

The PERA statutory funding resources are:

- member contributions (fixed statutory rates);
- affiliated public employer contributions (fixed statutory rates); and
- investment earnings of the PERA assets.

The basic funding objective of the PERA is to avoid transfers of the cost of statutory obligations between generations of taxpayers. This objective will be realized if the PERA funding resources are sufficient to finance:

- costs allocated to the current year attributable to service rendered by the PERA members in the current year (normal cost); and
- costs allocated to prior years attributable to service rendered by the PERA members in prior years (UAAL).

Board policy is to finance unfunded actuarial accrued liability over a period not to exceed 30 years. This policy was adopted in October 1996. The actuarial valuation measures: (1) the relationship between the PERA obligations and funding resources to determine if the funding objective is being met; and (2) the contribution rate needed to comply with the 30-year objective for financing the UAAL. The June 30, 2007 actuarial valuation indicates that the PERA funding resources are sufficient to fund the normal cost and finance the UAAL over an aggregate period of 13 years.

Mr. Slattery noted that the PERA's overall funded ratio is 93% with a $930 million unfunded liability.

Representative Bratton asked if each fund is independent or if fund balances can be moved from one plan to another. Mr. Slattery responded that within the PERA family of plans, funds can be moved; however, the judiciary and legislative plans are completely stand-alone and those fund balances cannot be moved.

Representative Powdrell-Culbert asked what happens to retirement contributions when a police officer is killed in the line of duty. Mr. Slattery responded that the PERA provides a lifetime death benefit to a beneficiary or, if no beneficiary has been designated, the PERA pays the employee contributions to the estate.

Mr. Slattery noted that the nine new positions authorized by the legislature last year have all been filled and that data purification on some 50,000 records is in progress.

Representative Varela asked what action is recommended to address the unfunded liability in the judicial plan. Mr. Slattery stated that the board recommends that retirement contributions be funded through payroll and supplemented by docket fees. Currently, there is a gap of 7.5% between actual contributions and the annual required contribution.

Representative Larrañaga asked about the outlook for the solvency of the PERA. Mr. Gish stated that the definition of a "mature fund" is one in which the benefits being paid exceed annual contributions. Mr. Slattery responded that the PERA is designed to pay benefits in perpetuity.

PERA Service Credit for Legislative Employees
—Steven Arias, Chief Clerk of the House

Mr. Arias presented the results of a 2005 survey, summarized as follows.

Arizona: Legislative Council has no session-only staff, only part-time employees, and most are retired. They do not receive benefits. In the House, full-time, session-only staff receive sick and vacation time as well as benefits (medical, vision, dental). They also can participate in a deferred compensation program. Most session-only staff are secretaries, and roughly 80 to 90% return each session. In order to retain the benefits offered by the state, during the interim the accounting department takes pay from employees via the vacation time they accrue during session. If employees' vacation times are depleted during the interim, they are allowed to pay for benefits out-of-pocket. If employees do not plan to return at the start of the next session, they can receive benefits via COBRA. Part-time, session-only staff (mostly pages) do not receive benefits. This method has not always been used and is subject to change, based on budget matters and leadership.

Colorado: Legislative Council has a small number of session-only staff and has been hiring retired personnel. Contracts with these employees have differed person to person. These employees can only work 110 days in order to retain their retirement benefits. The clerk's and secretary's offices hire most session-only staff. In the House, once session is over, session-only staff can elect to pay both the state share and the employee share to continue their benefits. A few full-time positions are shared by four session-only staff so that their benefits are covered.

Indiana: Part-time staff or temporary staff accrue vacation, sick, personal and holiday time at half the rate as full-time staff. They are not provided with medical, vision or dental benefits. Full-time, session-only staff receive benefits and pension, but only during the time period in which they work. They can collect unemployment when they are let go at the end of session.

Nevada: Session-only staff in Nevada receive insurance benefits if they work for at least three months. The insurance begins the first day of the month following three-months of employment. If employment is reinstated within one year of the termination date, the employee is classified as a reinstatement. The three-month waiting period is waived and coverage is effective on the first day of the month concurrent with or following the hire date. An employee who is rehired 12 months or more after the termination date, or who is rehired within 12 months but moves from a nonstate to a state agency. Coverage begins the first of the month following three months of full-time employment. If staff work for six months or more, they will be paid annual leave and employee or employer-paid retirement. (Most work from January until June or so.) The insurance coverage terminates on the last day of employment. Any state employee is offered this, and it can be found in Nevada's public employees benefit program (see link above). The coverage is for employees; however, they can opt to pay $5.00 or $10.00 from their paychecks to receive additional coverage for spouses or children. Employees can receive insurance after they leave legislative employment through COBRA.

New Hampshire: Examples of session-only staff in New Hampshire are committee secretaries and research secretaries. These employees are not provided benefits.

Ohio: Ohio does not employ session-only staff. Part-time staff receive benefits as if they are full-time staff; however, they accrue benefits such as vacation and sick time at a rate proportional to the amount they work.

Oregon: Oregon's benefit plan changes every session, depending upon factors such as the budget, managers, the current benefit plan for full-time staff and leadership. There is always something provided for session-only staff. The benefits plan is the same, regardless of position and place of employment within the legislature. In 2005, session-only staff received the same benefits as continuing employees, which was full coverage (i.e., medical, dental, vision). These benefits were available to the employee only. The state contribution ended at the end of session; however, employees could continue to receive benefits through COBRA.

South Dakota: South Dakota does not provide benefits to session-only employees, only salaries.

Mr. Arias stated that approximately 25 session employees in the House would be eligible for the proposed vested benefit plan.

Senator Rawson observed that legislative employees are not paid time-and-a-half for overtime.

New Mexico Film Investments; House Memorial 43
—Eric Witt, Director, Legislative/Political Affairs, Office of the Governor

The state of New Mexico has been remarkably successful in attracting film and television production to the state through an impressive array of financial incentives, so much so that it has become a preeminent destination for movies shot outside of California. Last year, the state recorded close to one-half billion dollars in economic impact from film production. Through a wide range of educational programs, the state has already begun educating students and local filmmakers to work not only on film projects in New Mexico, but also to initiate them.

In an effort to build further on the local film industry, House Memorial 43 (Representative Peter Wirth, 2007 regular session) requested that the administration work with representatives of the New Mexico film community to examine possible financial structures to support and enable resident, smaller-cap, independent filmmakers to produce feature films in the state. The working group's resulting proposal, set forth below, would provide financial incentives specifically targeted to New Mexico resident filmmakers and underrepresented filmmakers outside of the state. It may also provide an opportunity for the state to establish a significant presence in the Hispanic and Native American film markets by bringing a growing niche of minority filmmakers to New Mexico. The ideas set forth below are the results of the working group's deliberations in response to House Memorial 43 and do not necessarily reflect the position of the administration. Suggestions include:

- New Mexico filmakers production fund: A $25 million, zero-interest loan fund to provide production funding for local filmmakers and underrepresented minority filmmakers for films in New Mexico. Because of relaxed qualifying criteria, this fund would likely have to be established by a general fund allocation as opposed to the permanent fund, which is the funding source of the current production investment loan program.

- Investment tax credit: Establish a 10% tax credit available to individuals or corporations with New Mexico tax liability, in return for an investment in a local New Mexico film production or a New Mexico film fund.

The goals are to:

- increase participation of both independent New Mexico filmmakers and underrepresented minority filmmakers in the local film industry; and
- promote professional training for New Mexico residents in the entertainment industry, both above- and below-the-line.

Mr. Witt stated that the administration does not necessarily support the recommendations contained in the report.

Representative Powdrell-Culbert observed that it is not the state's responsibility to finance a hobby.

Representative Bratton is opposed to a $25 million appropriation for film projects that do not meet the prudent investor criteria.

Senator Smith noted that the latest consensus forecast is showing a slowing in revenue growth and there are serious needs for increased funding.

Review of Proposed Legislation
—Cleo Griffith, LCS

- House Bill 313 (return to work);
- House Bill 315 (IPOC);
- House Bill 532 (state treasurer; local government investment pool); and
- Senate Joint Memorial 6 (moratorium on benefit enhancements).

Representative Saavedra noted that Senator Rawson's bill might be subject to political problems in that the speaker and/or the pro tem might want to make the appointment rather than allowing the LFC to make the appointment.

Representative Trujillo observed that the proposed legislation might be viewed as an infringement on the powers of the executive.

Representative Bratton stated that he believes that members of the IPOC should attend financial seminars each year in order to exercise oversight properly.

Mr. Wollman stated that the State Investment Council (SIC) has an open door policy and is always willing to meet with legislators to educate them and answer questions.

Senator Smith recalled that the LFC identified problems in the State Treasurer's Office five to seven years before the problems finally became public and notified the attorney general, federal prosecutor and others. However, the LFC had no enforcement authority and nothing was ever done.

The committee requested that financial qualifications for the proposed new SIC board member be defined in the bill, and then the bill will be considered at the special meeting on December 11, 2007.

Senator Smith asked if there is any support for reintroducing the moratorium on retirement benefit enhancements. There was no support and the moratorium will not be endorsed.

The committee deferred action on the creation of a permanent IPOC until a special meeting of the committee on December 11, 2007.

The committee endorsed the treasurer's proposed legislation.

The committee endorsed the proposed "return-to-work" legislation.

Bill sponsors will be assigned at the December 11, 2007 meeting.

Other Business

Representative Saavedra discussed the potential combining of interim committees.

There was no other business brought before the committee.

The committee adjourned at 4:00 p.m.